



Federal Accounting Standards Advisory Board

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October 1, 2004

Memorandum

To: Members of the Board

From: Eileen Parlow, Assistant Director

Through: Wendy M. Comes, Executive Director

Subj: ***Accounting for Fiduciary Activities***<sup>1</sup>

## MEETING OBJECTIVE

The objectives of the proposed Fiduciary Activities standard are:

- To improve the public's understanding of the concepts of "trust funds" by establishing clear definitions, terminology and reporting standards for programs designated as "trust funds" or "special funds" in the budget, as well as fiduciary activity, which resembles private sector "trust fund" activity. The "Earmarked Funds" standard addressed funds categorized as "trust funds" and "special funds" in the budget; the proposed Fiduciary Activities standard addresses activities that resemble private sector "trust fund" activity.
- To improve accountability for non-Federal nonentity collections and assets.
- To develop reporting standards that clearly distinguish between Government-owned and non-Federal nonentity collections, assets, and the related liabilities.

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<sup>1</sup> The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

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## Attachment A: Discussion of Questions

To further these objectives, staff recommends that the Board consider the following:

1. Should non-Federal nonentity assets and offsetting liabilities be moved from the Balance Sheet to a proposed new principal statement, the Statement of Fiduciary Accountability? The proposed statement would also report flows related to the balances. (Page 3)
2. If so, should the Statement of Fiduciary Accountability also be included as a principal statement in the Government-wide statements? (Page 4)
3. Regardless of (1) and (2) above, should the proposed Fiduciary Activities standard address all funds held by Federal agencies that are not Government-owned? (Page 5)

## Attachments:

Attachment A: Discussion of Questions

Attachment B: Pro Forma Statements of Fiduciary Accountability

Tab 1: Original exposure draft, *Accounting for Fiduciary Activities*, with proposed changes marked (Preliminary draft for re-exposure).

Tab 2: OMB Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, Transmittal Letter and Sections 1-7.

Tab 3: List of deposit funds and balances from the U.S. Treasury's FY 2003 Annual Report

**Note: The Board also received a separate briefing binder with historical and reference materials relating to fiduciary activities.**

## Attachment A: Discussion of Questions

**Question 1:** Should non-Federal nonentity assets and offsetting liabilities be moved from the Balance Sheet to a proposed new Statement of Fiduciary Accountability? The proposed statement would also report flows related to the balances. (Examples of two possible statement formats are at Attachment B to this memorandum.)

**Staff recommendation:** Staff recommends that non-Federal<sup>2</sup> nonentity assets and offsetting liabilities be moved from the Balance Sheet to a proposed new Statement of Fiduciary Accountability. Below are pros and cons for this recommendation.

### **Pros:**

- Several Board members, as well as respondents to the Fiduciary Activities ED, have questioned the placement of assets that are not government-owned (non-Federal nonentity assets) on the government entity's Balance Sheet. Currently, the distinction between entity and non-entity<sup>3</sup> assets is disclosed in the notes, and not on the face of the financial statements. Nonentity assets are required to be segregated from entity assets<sup>4</sup> in the financial statements. The pro forma Balance Sheet in SFFAC 2, *Entity and Display*, illustrates separation of entity versus nonentity assets on the face of the statement. However, OMB's *Form and Content* directs that the distinction be disclosed in the notes, and not on the face of the Balance Sheet. The placement of non-Federal nonentity assets on a separate principal statement would clearly distinguish between assets that are government-owned and assets that are not government-owned, without increasing the "clutter factor" of the component entity's balance sheet.
- A principal financial statement, such as the proposed Statement of Fiduciary Accountability, would provide a more prominent display that is more accessible to beneficiaries and other readers than note disclosure.
- A principal financial statement, such as the proposed Statement of Fiduciary Accountability, would provide audit assurance for the fiduciary information reported.
- The proposed Statement of Fiduciary Accountability would provide an appropriate venue for reporting fiduciary activity for agencies that are currently using the Statement of Custodial Activity (SCA) to report fiduciary collections. The SCA was originally intended by the Board to report on intragovernmental activity. SFFAC 2, *Entity and Display*, excludes non-Federal nonentity collections from the SCA.<sup>5</sup> For

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<sup>2</sup> **Non-Federal** nonentity assets are assets that are not government-owned. **Federal** nonentity assets are assets that are not available to the component agency, but are available to another component within the Federal government.

<sup>3</sup> "**Entity assets** are those assets which the reporting entity has authority to use in its operations. **Non-entity assets** are those assets that are held by an entity but are not available to the entity." (SFFAS 1, par. 25)

<sup>4</sup> SFFAS 1, par. 26

<sup>5</sup> "Custodial collections do not include deposit funds, i.e. amounts held temporarily by the Government (e.g., bidders' earnest money or guarantees for performance) or amounts held by the Government as an agent for others (e.g., state income taxes withheld from Federal employees' salaries that are to be transferred to the states)." (SFFAC 2, par. 102)

## Attachment A: Discussion of Questions

this reason, the Board did not anticipate the expanded use of the SCA to report fiduciary activities performed by the Government on behalf of non-Federal parties. If the proposed standard were adopted, the Statement of Custodial Activity would be restored to its original purpose.

### **Cons:**

- The preparation and audit of an additional principal statement might generate additional expenses, such audit expense, to the component agencies. However, some of the information required is currently reported on the Federal agency's Balance Sheet and/or Notes.
- Since there would now be two principal statements (Custodial and Fiduciary) that may be absent from a Federal agency's financial statements, the Board may wish to address materiality in the context of whether to require the Fiduciary statement (and/or the Custodial statement) regardless of materiality. For example, GASB 34 requires fiduciary fund statements, and does not exempt state or local governments from preparing the statements on the basis of materiality.
- OMB Bulletin 01-02, Audit Requirements for Federal Financial Statements and Bulletin 01-09, Form and Content of Agency Financial Statements, should be updated to include the new principal statement.

**Question 2:** If the proposed Statement of Fiduciary Accountability is approved, should it also be included as a Government-wide statement?

**Staff recommendation:** Staff recommends that the proposed Statement of Fiduciary Accountability be added as a Government-wide financial statement for the following reasons:

### **Pros:**

- The Statement of Fiduciary Accountability relates to a fiduciary relationship between the Federal Government and non-Federal individuals or entities. Unlike custodial activities, fiduciary activities are not eliminated in the consolidation process.
- It is likely that some fiduciary activities are qualitatively and/or quantitatively material to the Government-wide financial statements.

### **Cons:**

- The preparation and audit of an additional principal statement might generate additional expenses.

**Question 3:** Should the proposed Fiduciary Activities standard address all funds held by Federal agencies that are not Government-owned?

The definition that appears in the original ED would include all deposit funds.<sup>6</sup> Deposit funds are reported to Treasury but are not included in the Budget of the U.S. Government. In addition to the Indian funds and the Thrift Saving Fund investments in Treasury securities, deposit funds include certain advances from non-Federal parties and payroll withholdings due to state and local governments.

**Question for the Board:** Is it the Board's intention that the variety of activities represented by deposit funds be included in the reporting requirements for Fiduciary Activities?

***Note: A list of deposit funds and balances appears at Tab 3.***

**Pros:**

- Establishing clear reporting requirements for all deposit funds would improve the completeness and quality of reporting to Treasury for deposit funds, which would enhance the quality of information available for the preparation of the Government-wide financial report.
- If the Board decides in the affirmative for (1) and (2) above:
  - Non-Federal nonentity assets would no longer be combined with Government-owned assets on the Balance Sheet; instead they would be reported on the Statement of Fiduciary Accountability.
  - Since all deposit funds would be reported on a principal financial statement, deposit funds would be subject to audit scrutiny. This might enhance the quality of information available to Treasury for the preparation of the Government-wide financial report.
- If the Board decides to include deposit funds, the original definition criteria for fiduciary activities will not need to be modified. [The attached revised ED illustrates how the criteria and characteristics might be modified to exclude payroll tax clearing accounts and similar deposit funds.]

**Cons:**

- The preparation and audit of an additional principal statement might generate additional expenses, such as audit expenses, to the component agencies.
- Some deposit funds, such as payroll withholdings due to state and local governments or other non-Federal parties, are beyond the scope of the original

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<sup>6</sup> See note 5 for a definition of deposit funds.

## Attachment A: Discussion of Questions

purpose of the Fiduciary Activities project, which was the fiduciary portion of “dedicated collections.”

- “Dedicated collections” are subject to special accountability because they are either (a) earmarked funds, or (b) not government-owned. However, some deposit funds, such as those used for payroll withholdings of state and local taxes, were funded by general appropriations and were government-owned until the time of payment into the deposit fund. The inclusion of all deposit funds as “fiduciary activities” might require a rule-based standard in order to distinguish between certain deposit funds and general government activity.

**Staff recommendation:** Staff recommends that the Board consider the pros and cons above.

Attachment B: Pro Forma Statement of Fiduciary Accountability

**EXAMPLE A: FINANCIAL STATEMENT FORMAT, NET ASSETS MODEL**

STATEMENT OF FIDUCIARY ACCOUNTABILITY

For the period ended September 30, XXXX

**Fiduciary Net Assets as of September 30, XXXX**

FIDUCIARY ASSETS

Cash and investments	\$	XX
Cash held as Fund Balance with Treasury		XX
Cash held outside of the U.S. Treasury		XX
Investments in Treasury securities		XX
Investments in non-Federal securities		XX
Seized monetary assets		
Other assets		
Other fiduciary assets		<u>XX</u>

TOTAL FIDUCIARY ASSETS	\$	<u>XXXX</u>
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LESS: FIDUCIARY LIABILITIES

Accounts Payable	\$	<u>XX</u>
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NET FIDUCIARY ASSETS	\$	<u>XXXX</u>
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**Increase (Decrease) in Net Assets for the period ended September 30, XXXX**

COLLECTIONS:

Collected from beneficiaries	\$	XX
Interest and other revenues from fiduciary assets		XX
Other fiduciary receipts		XX
Less: Investment and other losses		<u>(XX)</u>

TOTAL COLLECTIONS	\$	<u>XXXX</u>
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DISPOSITION OF COLLECTIONS

Paid to beneficiaries	\$	XX
Paid for administrative expenses		<u>XX</u>

TOTAL DISPOSITION OF COLLECTIONS	\$	XXX
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INCREASE (DECREASE) IN NET ASSETS	\$	XXX
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Net Assets, Beginning of Period	\$	XXXX
Increase (Decrease) in Net Assets		<u>XXX</u>
Net Assets, End of Period	\$	<u>XXXX</u>

**EXAMPLE B: FINANCIAL STATEMENT FORMAT, ASSETS = LIABILITIES MODEL**

STATEMENT OF FIDUCIARY ACCOUNTABILITY

For the period ended September 30, XXXX

**Fiduciary Assets and Liabilities as of September 30, XXXX**

FIDUCIARY ASSETS

Cash and investments	\$	XX
Cash held as Fund Balance with Treasury		XX
Cash held outside of the U.S. Treasury		XX
Investments in Treasury securities		XX
Investments in non-Federal securities		XX
Seized monetary assets		
Other assets		
Other fiduciary assets		<u>XX</u>

TOTAL FIDUCIARY ASSETS \$ XXXX

FIDUCIARY LIABILITIES

Accounts Payable	\$	XX
Due to beneficiaries		<u>XX</u>

TOTAL FIDUCIARY LIABILITIES \$ XXXX

**Fiduciary Collections and Dispositions for the period ended September 30, XXXX**

COLLECTIONS:

Collected from beneficiaries	\$	XX
Interest and other revenues from fiduciary assets		XX
Other fiduciary receipts		XX
Less: Investment and other losses		<u>(XX)</u>

TOTAL COLLECTIONS \$ XXXX

DISPOSITION OF COLLECTIONS

Paid to beneficiaries	\$	XX
Paid for administrative expenses		XX
Retained for future disposition		<u>XX</u>

TOTAL DISPOSITION OF COLLECTIONS \$ XXXX